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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935.

NO. 273.

COMMONWEALTH TRUST COMPANY OF PITTSBURGH, Trustee, and THOMAS B. MacMILLAN, JOHN L. BRENTZELL, JANE B. WHEELER and ANNA L. MEYER, Petitioners,

v.

ARTHUR R. ATWOOD, Receiver of THE BANK OF PITTSBURGH NATIONAL ASSOCIATION, in Lieu of C. O. THOMAS, Receiver at the Time Suit was Brought, Respondent.

BRIEF FOR RESPONDENT.

JOHN G. FRAZER,
747 Union Trust Building,
Pittsburgh, Pennsylvania,
Counsel for Respondent.

ROBERT L. KIRKPATRICK,
747 Union Trust Building,
Pittsburgh, Pennsylvania,
Of Counsel.

SMITH BROS. CO. INC., LAW PRINTERS, 208-212 GRANT STREET, PITTSBURGH, PA.

INDEX.

	PAGE
Brief for Respondent	1
Counter-Statement of the Matters Involved	1
Argument	6
I. The District Court Had Jurisdiction and Properly Refused to Surrender It in Favor of the State Court	6
(A) The Exercise of Its Jurisdiction by the District Court	6
(B) Respondent Is Not Required to Account to the State Court	12
(C) Petitioners' Authorities on the Question of Jurisdiction	15
II. The Case Was Properly Determined on the Merits	18
(A) The Allowance of Interest Is Not in Conflict with the Decision of the Circuit Court of Appeals for the Eighth Circuit	18
(B) The Operation of the Mortgage Pool Was Lawful and No Question of Impropriety Is Presented by the Record	20
III. All the Indispensable Parties Were Before the Court	23

Cases Cited.

	PAGE
Art Students League v. Hinkley, 31 Fed. (2d) 469	11
Byers v. McAuley, 149 U. S. 608, 37 L. Ed. 867	16
Commonwealth of Pennsylvania v. Williams, 293 U. S. ...., 79 L. Ed. 384 (1935)	15
Edward Hines Yellow Pine Trustees v. Martin, 268 U. S. 458, 465, 69 L. Ed. 1050, 1054 (1925)	14, 20
First Trust Company of Lincoln v. Ricketts, 75 Fed. (2d) 309 (C. C. A. 8th)	18
Gibson v. Peters, 150 U. S. 242	7
Harrison v. Moncravie, 264 Fed. 776	11
Kerrison v. Stewart, 93 U. S. 155, 23 L. Ed. 843 (1876)	23
Larsen v. Bank and Trust Company, 178 Minn. 209	22
Penn General Casualty Company v. Commonwealth of Pennsylvania, 293 U. S. ...., 79 L. Ed. 392 (1935)	15
People's Trust Company v. United States, 23 Fed. (2d) 381	17
Primeau v. Granfield, 193 Fed. 911 (C. C. A. 2nd) (1911)	22
Riehle v. Margolies, 279 U. S. 218, 73 L. Ed. 669 (1929)	10
Smith v. Swormstedt, 16 How. 288, 14 L. Ed. 942 (1853)	23
Ulmer v. Fulton, Superintendent of Banks, 129 Ohio State 323	22
Waterman v. Canal-Louisiana Bank & Trust Company, 215 U. S. 33, 43, 54 L. Ed. 80, 84 (1909)	7
Yonley v. Lavender, 21 Wall. 276, 22 L. Ed. 536	16

Authorities.

	PAGE
Equity Rule 38	23
General Incorporation Act of Pennsylvania of April 29, 1874, P. L. 73	20
Opinion of Attorney General of Pennsylvania, 27 District Reports 986	20
Pennsylvania Act of April 6, 1925, P. L. 152 (15 P. S. 2514)	2, 20
Pennsylvania Act of May 9, 1889, P. L. 159	20
Pennsylvania Banking Code of 1933	1, 20
Section 11 (k) of Federal Reserve Act (12 U. S. C. A. 248 (k))	20
Section 24 (1) of the Judicial Code, 28 U. S. C. A. 41 (1)	6
Section 24 (16), 28 U. S. C. A. 41 (16)	6

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v.

ARTHUR R. ATWOOD, Receiver of THE BANK OF PITTSBURGH NATIONAL ASSOCIATION, in Lieu of C. O. THOMAS, Receiver at the Time Suit was Brought, Respondent.

BRIEF FOR RESPONDENT.

COUNTER-STATEMENT OF THE MATTERS INVOLVED.

The questions involved in this case are not of wide and public interest or of public importance but are of concern only to the parties. The case is controlled by its own peculiar facts as will appear by a brief review of the essential facts as they appear in the pleadings and the agreed statement of facts upon which the case was submitted.

Prior to July 3, 1933, the effective date of the Pennsylvania Banking Code (Act of May 15, 1933, P. L.

624), there was in effect in Pennsylvania a statute approved April 6, 1925, P. L. 152, and the amendments and supplements thereto, which gave banks and trust companies the right to

> "assign to their various trust estates participation in a general trust fund of mortgages upon real estate securing bonds, in which case it shall be a sufficient compliance with the provisions of this section for the company to designate clearly on its records the bonds and mortgages composing such general trust fund, the names of the trust estates participating therein, and the amounts of the respective participations; and in such case no estate so participating shall be deemed to have individual ownership in any bond and mortgage in such fund, and the company shall have the right at any time to repurchase at market value but not less than face value any such bonds and mortgages from such fund, with the right to substitute therefor other bonds and mortgages."

The Bank of Pittsburgh National Association, hereinafter called the "Bank", pursuant to the authority conferred by this Act, established and maintained a general trust fund of mortgages upon real estate, which mortgages were held by its Trust Department and segregated from the general assets of the Bank (R. 26).

When a mortgage was purchased for the trust fund and was delivered to the Bank, it was "thereupon" placed in the general trust fund, hereinafter called the "Mortgage Pool", and the Bank executed a certificate describing the mortgage and certifying that it was held by the Trust Department "in trust for those of its customers who have purchased participations therein" (R. 26-27). Participation Certificates were sold from time to time to various customers of the Bank, including

trusts of the Bank. These certificates set forth the name of the customer, the date, an amount stated in dollars, and certified that "the above estate is a participant to the extent of the amount indicated above" (R. 27).

The aggregate face value of mortgages in the Mortgage Pool at all times exceeded the aggregate face value of the participations, the excess varying from day to day. On September 21, 1931, the date of the closing of the Bank, the aggregate face value of mortgages in the Mortgage Pool was $5,347,585.57, and of the outstanding certificates, $5,056,565.12. No Participation Certificates had been issued to the Bank, and no payment had been made to it, for the excess of $291,020.45 (R. 28).

The Trust Department collected interest as it became payable on the mortgages in the Mortgage Pool, and paid interest, at the rate of 6% per annum, less Trustee's commission and taxes, to holders of participations, quarter-annually on the 15th days of February, May, August and November. Interest was paid to the Bank monthly at the rate of 6% per annum on the amount by which the mortgages in the Pool exceeded the outstanding Participation Certificates. The interest due to certificate holders on August 15, 1931, approximately a month prior to suspension, exceeded mortgage interest collected by $57,156.76 and this amount was advanced by the Bank to the Mortgage Pool. The amount so advanced was reduced to $40,213.58 at the time of closing by additional collections of interest between August 15th and the date of closing (R. 28-29).

On January 19, 1932, a Petition was presented to the Orphans' Court of Allegheny County, Pennsylvania, by the holder of a Participation Certificate, averring that all trusts holding certificates were subject to the

jurisdiction of the Orphans' Court except certain trusts subject to the jurisdiction of the Court of Common Pleas, all of which had consented, and that Respondent's predecessor desired to be relieved of the custody of the Mortgage Pool. The Petition prayed that the Bank be removed as Trustee and a substitute Trustee appointed. The Court then declared that an emergency existed by reason of the closing of the Bank and removed the Bank as Trustee of the Mortgage Pool and appointed Commonwealth Trust Company of Pittsburgh, one of the Petitioners herein, as successor Trustee, and the assets of the Mortgage Pool were transferred to it (R. 29-30). The Receiver did not join in this Petition as stated by Petitioners (Petition, page 4).

Payments on account of principal and interest have been made from time to time by the successor Trustee to the holders of Participation Certificates but no payments were made by it to Respondent. Therefore, Respondent, in order to secure a judicial determination of his rights, filed a Bill in Equity against the successor Trustee and the other Petitioners herein who were joined as defendants as representatives of all holders of certificates. The Bill averred (R. 4), the Answer admitted (R. 20) and in the Agreed Statement of Facts it is stipulated that the holders of Participation Certificates "are joined herein as defendants as representatives of all holders of certificates * * * the holders of such certificates being so numerous and so widely scattered that it would be impracticable to bring them all before the Court in this proceeding, and the rights of all certificate holders being the same" (R. 25). Petitioners moved to dismiss the Bill on the ground that the Court was without jurisdiction, which motion was denied in an Opinion and Order of Court filed June 12, 1933 (R. 15). The case was put down for trial and heard on an Agreed Statement of Facts which the par-

ties stipulated should be accepted in lieu of testimony. The District Court entered a decree adjudging that there was due and payable to Respondent the unpaid portion of the amount advanced to pay interest; that Respondent was a participant to the amount of $291,020.45 and, therefore, entitled to share proportionally with the holders of certificates; and ordered the Trustee to pay to Respondent certain sums withheld from him under previous distributions to holders of Participation Certificates. The Circuit Court of Appeals affirmed but modified the decree of the District Court by striking out the order to the Commonwealth Trust Company of Pittsburgh, Trustee, to pay any of the claims forthwith. A Petition for Reargument was denied without opinion.

These facts, established by admissions in the pleadings and the Agreed Statement of Facts submitted to the Court but not fully set forth in the Petition, show that the case is really *sui generis* and does not possess a single feature essential to a review on a certiorari. However, the broad principles advanced and argued by Petitioner will be considered as briefly as possible.

ARGUMENT.

Petitioners' argument consists of six divisions. Points I, II and III concern the jurisdiction of the District Court and the exercise of that jurisdiction. Points IV and V question the decision of the courts below on what may be called the merits of the case and Point VI deals with the question of parties defendant.

I.

The District Court Had Jurisdiction and Properly Refused to Surrender It in Favor of the State Court.

Points I, II and III will first be discussed.

(A)

THE EXERCISE OF ITS JURISDICTION BY THE DISTRICT COURT.

Petitioners' argument on the question of jurisdiction is based not only upon an erroneous conception of the facts of the case but also upon a failure to recognize that the nature of the jurisdiction exercised by the District Court is *in personam* and not *in rem*.

It is elementary that the statutes of the United States are controlling as to the jurisdiction and venue of suits in the Federal courts. Section 24 (1) of the Judicial Code, 28 U. S. C. A. 41 (1), provides that the district courts shall have original jurisdiction "of all suits of a civil nature, at common law or in equity, brought by the United States, or by any officer thereof authorized by law to sue * * *", and Section 24 (16), 28 U. S. C. A. 41 (16), provides that they shall have jurisdiction "of all cases commenced by the United States, or by direction of any officer thereof, against any national banking association, and cases for winding up

the affairs of any such bank." The proceeding in the District Court was a bill in equity filed by the receiver of a national bank who is an officer of the United States; *Gibson v. Peters,* 150 U. S. 242. It is, therefore, clear that the District Court has jurisdiction of the cause.

The mere fact that the Respondent did not object to the appointment by the State Court of a successor Trustee for a voluntary trust already existing and created wholly independent of that Court, does not preclude the District Court from exercising its otherwise clearly defined power. Petitioners' argument is much weaker than would be the case if the trust were testamentary or the action against an administrator, an executor or a receiver deriving powers under the appointment of a State Court. It is well settled, however, that the Federal courts have jurisdiction to entertain suits, even against such fiduciaries, where the requisites of Federal jurisdiction exist, for the purpose of establishing claims against the estates involved and to secure a determination of the rights of the parties claiming an interest in them. The matter before the Court in such a case is not the collection of the amount of a judgment or decree but whether or not the plaintiff is entitled to establish his claim by a judgment or decree. The judgment or decree of the Federal Court in such a case does not purport to deal with the property.

The applicable law is stated by Mr. Justice Day in *Waterman v. Canal-Louisiana Bank & Trust Company,* 215 U. S. 33, 43, 54 L. Ed. 80, 84 (1909) as follows:

> "From an early period in the history of this court, cases have arisen requiring a consideration and determination of the jurisdiction of the courts of the United States to entertain suits against administrators and executors *for the purpose of establishing claims against estates, and to have a de-*

termination of the rights of persons claiming an interest therein. And this court has had occasion to consider how far the jurisdiction in equity of the courts of the United States in such matters may be affected by the statutes of the states providing for courts of probate for the establishment of wills and the settlement of estates. We will not stop to analyze or review in detail all these cases, as they have been the subject of frequent and recent consideration in this court. The general rule to be deduced from them is that, inasmuch as the jurisdiction of the courts of the United States is derived from the Federal Constitution and statutes, that, in so far as controversies between citizens of different states arise which are within the established equity jurisdiction of the Federal courts, which is like unto the high court of chancery in England at the time of the adoption of the judiciary act of 1789 (1 Stat. at L. 73, chap. 20), the jurisdiction may be exercised, and is not subject to limitations or restraint by state legislation establishing courts of probate, and giving them jurisdiction over similar matters. *This court has uniformly maintained the right of Federal courts of chancery to exercise original jurisdiction (the proper diversity of citizenship existing) in favor of creditors, legatees, and heirs, to establish their claims and have a proper execution of the trust as to them.* In various forms these principles have been asserted in the following, among other, cases: *Suydam v. Broadnax,* 14 Pet. 67, 10 L. ed. 357; *Hyde v. Stone,* 20 How. 170, 175, 15 L. ed. 874, 875; *Green v. Creighton (Kendall v. Creighton),* 23 How. 90, 16 L. ed. 419; *Payne v. Hook,* 7 Wall. 425, 19 L. ed. 260; *Lawrence v. Nelson,* 143 U. S. 215, 36 L. ed. 130, 12 Sup. Ct. Rep. 440; *Hayes v. Pratt,* 147 U. S. 557, 570, 37 L. ed.

279, 284, 13 Sup. Ct. Rep. 503; *Byers v. McAuley,* 149 U. S. 608, 37 L. ed. 867, 13 Sup. Ct. Rep. 906; *Ingersoll v. Coram,* 211 U. S. 335, 53 L. ed. 208, 29 Sup. Ct. Rep. 92.

"The rule stated in many cases in this court affirms the jurisdiction of the Federal Courts to give relief of the nature stated, notwithstanding the statutes of the state undertake to give to state probate courts exclusive jurisdiction over all matters concerning the settlement of accounts of executors and administrators in the distribution of estates. This rule is subject to certain qualifications, which we may now notice. The courts of the United States, while they may exercise the jurisdiction, and may make decrees binding upon the parties, cannot seize and control the property which is in the possession of the state court. In *Byers v. McAuley, supra,* the rule was thus tersely stated by Mr. Justice Brewer, delivering the opinion of the court:

" 'A citizen of another state may establish a debt against the estate. *Yonley v. Lavender,* 21 Wall, 276, 22 L. ed. 536; *Hess v. Reynolds,* 113 U. S. 73, 28 L. ed. 927, 5 Sup. Ct. Rep. 377. But the debt thus established must take its place and share of the estate as administered by the probate court; and it cannot be enforced by process directly against the property of the decedent. *Yonley v. Lavender, supra.* In like manner, a distributee, citizen of another state, may establish his right to a share in the estate, and enforce such adjudication against the administrator personally, or his sureties (*Payne v. Hook,* 7 Wall. 425, 19 L. ed. 260); or against any other parties subject to liability (*Borer v. Chapman,* 119 U. S. 587, 30 L. ed. 532, 7 Sup. Ct. Rep. 342), or in any other way which does not dis-

turb the possession of the property by the state court. (See the many cases heretofore cited.)'" (Italics ours).

The principles established by the Federal Courts in cases of receivership should also be noticed. Proceedings for the appointment of a receiver are *quasi in rem,* and the court appointing the receiver takes into its possession and custody the assets involved. The possession and control of the receiver is the possession and control of the court, but even in such instances it is well settled that a court of competent jurisdiction is not precluded from establishing a claim or rendering the judgment which establishes the right to participate in the distribution of property in the possession of another court. The leading case is *Riehle v. Margolies,* 279 U. S. 218, 73 L. Ed. 669 (1929). In it, Mr. Justice Brandeis said:

"The contention that the judgment is not conclusive rests upon the argument that, because the appointment of the receiver draws to the appointing court control of the assets and in the distribution of them among creditors there is necessarily involved a determination both of the existence of the claim and of the amount of the indebtedness, the federal court must have the exclusive power to make that determination. The argument ignores the fact that an order which results in the distribution of assets among creditors has ordinarily a two-fold aspect. In so far as it directs distribution, and fixes the time and manner of distribution, it deals directly with the property. *In so far as it determines, or recognizes a prior determination of the existence and amount of the indebtedness of the defendant to the several creditors seeking to participate, it does not deal directly with any of the property. The latter function, which is spoken of as the*

liquidation of a claim, is strictly a proceeding in personam. (Italics ours).

* * * * * * *

"The establishment of a claim constituting the basis of the right to participate in the distribution of property in the possession of one court is often conclusively determined by a judgment obtained in another court. Thus, a judgment of a federal court may establish conclusively the fact which entitles one to share in a decedent's estate in course of administration in a state court. *Yonley v. Lavender,* 21 Wall. 276, 22 L. ed. 536; *Hess v. Reynolds,* 113 U. S. 73, 28 L. ed 927, 5 Sup. Ct. Rep. 377; *Byers v. McAuley,* 149 U. S. 608, 620, 37 L. ed. 867, 873, 13 Sup. Ct. Rep. 906; *Waterman v. Canal-Louisiana Bank & T. Co.,* 215 U. S. 33, 54 L. ed. 80, 30 Sup. Ct. Rep. 10. Under the Bankruptcy Act of (March 2), 1867 (14 Stat. at L. 517, chap. 176), a judgment against the debtor rendered in a suit in a state court pending at the time of the commencement of the bankruptcy proceedings established conclusively in bankruptcy the existence and amount of the debt provable against the estate. *Norton v. Switzer,* 93 U. S. 355, 363, 364, 23 L. ed. 903, 906, 907. Compare *Hill v. Harding,* 107 U. S. 631, 27 L. ed. 493, 2 Sup. Ct. Rep. 404."

See also *Harrison v. Moncravie,* 264 Fed. 776; *Art Students League v. Hinkley,* 31 Fed. (2d) 469.

The object of Respondent's Bill was to establish the existence, amount and characteristics of his claims. The question which the Federal Court was asked to adjudicate was what, if any, obligation the successor Trustee owed the Receiver. The Bill did not ask the Federal Court to make distribution of the trust funds but merely to establish the claim. The matter of dis-

tribution must be under the jurisdiction of the Orphans' Court and there can be no question, as suggested by Petitioners, as to which Court the Trustee shall obey.

(B)

RESPONDENT IS NOT REQUIRED TO ACCOUNT TO THE STATE COURT.

Petitioners assert that the operation of the Mortgage Pool was an illegal transaction; that Respondent is obliged to file accounts with the State Court covering its management of the Mortgage Pool and various trust estates; and that the adjudication of the District Court will preclude the State Court from determining the many questions which, it is stated, "will undoubtedly arise" (Petition, page 6). There are several answers to Petitioners' suggestion.

Respondent is *not* required to file an account in the Orphans' Court or elsewhere as Trustee of the Mortgage Pool. Petitioners cite no statutes or cases to support their position. The Bank was not under the jurisdiction of that Court. It was not appointed Trustee of the Mortgage Pool by the State Court, nor was the trust created by any will or by the act of any person other than the Bank. The Receiver did not "procure an order to turn over the trust *res* to a successor trustee" as stated by Petitioners (Petition, page 11). The action was taken by a certificate holder and the Court acted under emergency authority given it by Pennsylvania Statutes. Under such circumstances there is no provision of Pennsylvania law which requires Respondent to account to the State Court, although of course any party having a right of action against the Bank for mismanagement of the Pool could sue the Receiver in any court having jurisdiction. Such a suit would, however, be removable by Respondent to the District Court. But in

almost four years no such suit has been instituted nor has any threat of such action been made.

If the Bank had been Trustee under a corporate mortgage and held in trust estates some of the bonds secured by that mortgage, it would not be obligated to account to the Orphans' Court as Trustee under the mortgage if the mortgagor should fail to meet its obligations. Yet this is an analagous situation.

Assuming an account should be filed by Respondent, Petitioners' argument proceeds on the assumption that the Respondent might then be surcharged upon the auditing of the account by the State Court and that this would defeat his claim. The argument also is unsound. A surcharge would result only in the establishment of a general claim against the Bank which Respondent would be obliged to allow and pay out of the general assets of the Bank. If a surcharge against the Bank as fiduciary for a specific estate established a liability against the Mortgage Pool, the effect would be to pay general claims of the Bank out of funds held in trust for numerous equitable owners. Any such doctrine would be revolutionary.

Furthermore, the suggestion of a conflict of jurisdiction by reason of alleged illegality in the operation of the Mortgage Pool is without foundation. There is not even a suggestion in the record that the operation of the Mortgage Pool was improper or that the Bank defaulted in any manner in the performance of its duties. No such question was raised either in the court below or in the Circuit Court of Appeals until the Petition for Reargument was filed. Therefore, this Court will not now consider that question.

Edward Hines Yellow Pine Trustees v. Martin, 268 U. S. 458, 465, 69 L. ed. 1050, 1054 (1925):

> "* * * This court is a court of review, and it will not consider questions not raised or disclosed by the record brought to it for review, and which were not considered by the courts below. *McClellan v. Carland,* 217 U. S. 268, 283, 54 L. ed. 762, 767, 30 Sup. Ct. Rep. 501; *Bass, Ratcliff & Gretton v. State Tax Commission,* 266 U. S. 271, 285 *ante,* 282, 288, 45 Sup. Ct. Rep. 82. And see *Davis v. Currie,* 266 U. S. 182, *ante,* 234, 45 Sup. Ct. Rep. 88, and *United States Fidelity & G. Co. v. Wooldridge,* decided May 11, 1925 (268 U. S. 234, *ante,* 932, 40 A. L. R. ——, 45 Sup. Ct. Rep. 489)."

As this question is now raised for the first time, fairness to the courts below and to the Respondent requires a corresponding departure by us from the record to state facts which would have been proven by us if the question had been raised at the trial. Respondent advises us that at the time of suspension, the Bank was acting as fiduciary for one hundred forty-seven court trusts, and that accounts have been filed, and Respondent discharged, in all but nine, which have not been closed for various reasons wholly unrelated to any question of surcharge by reason of the operation of the Mortgage Pool. In the case of personal trusts, we are advised that the number at the time of suspension was four hundred thirty-one, and that only five have not been closed for one reason or another, having no connection with the assertion of a surcharge. In no court or voluntary trust has any such question been raised by a beneficiary or by any court. Therefore, Petitioners' suggestion of a possible conflict of jurisdiction in the event of a surcharge is not only unsound on well established legal principles but imaginary as well.

(C)

PETITIONERS' AUTHORITIES ON THE QUESTION OF JURISDICTION.

It is clear that the principles applied in the cases of *Commonwealth of Pennsylvania v. Williams,* 293 U. S. ...., 79 L. Ed. 384 (1935), and *Penn General Casualty Company v. Commonwealth of Pennsylvania,* 293 U. S. ...., 79 L. Ed. 392 (1935), have no application to the facts presented by this record. The principle established by those cases is that, under certain circumstances, a Federal district court should, in the exercise of its discretion, relinquish its jurisdiction *to appoint receivers* in favor of proper *state officers* designated by statute for the *administration* of the assets of building and loan associations and insurance companies, where the procedure provided by statute is adequate and complete and accomplishes the same end in substantially the same manner as an equity receivership in the Federal Court. The cases turn on a desire to defer to the policy of the Commonwealth to *liquidate* such institutions by state *administrative officers.* Mr. Justice Stone makes this perfectly clear in the Williams case:

> "The question is not the ordinary one of comity between a federal and a state court, each asserting jurisdiction over the same subject matter, and the same property, and where there are shown no special reasons addressed to the discretion of the court first acquiring jurisdiction for relinquishing its jurisdiction in favor of the other. (Citing cases). Here no state court is asserting jurisdiction, but the state officer, charged by the statutes of the state with the duty of supervising its own building and loan associations and of liquidating them by an adequate procedure when insolvent, asks to proceed with the liquidation."

The Penn General Casualty case also points out the distinction in comity between courts of concurrent jurisdiction and yielding administration to a state administrative officer. Mr. Justice Stone said:

> "* * * While it is often said that of two courts having concurrent jurisdiction *in rem*, that one first taking possession acquires exclusive jurisdiction, see *Peck v. Jennes, supra* (7 How. 624, 625, 12 L. ed. 846, 847); *Wabash R. Co. v. Adelbert College, supra* (208 U. S. 54, 52 L. ed. 386, 28 S. Ct. 182); *Harkin v. Brundage, supra* (276 U. S. 43, 72 L. ed. 460, 48 S. Ct. 268), it is exclusive only so far as its exercise is necessary for the appropriate control and disposition of the property. The jurisdiction does not extend beyond the purpose for which it is allowed, to enable the court to exercise it appropriately and to avoid unseemly conflicts. See *Leadville Coal Co. v. McCreery, supra* (141 U. S. 477, 35 L. ed. 825, 12 S. Ct. 28). The other court does not thereby lose its power to make orders which do not conflict with the authority of the court having jurisdiction over the control and disposition of the property. *Yonley v. Lavender*, 21 Wall. 276, 22 L. ed. 536; *Heidritter v. Elizabeth Oil-Cloth Co.*, 112 U. S. 294, 304, 28 L. ed. 729, 733, 5 S. Ct. 135; *Byers v. McAuley*, 149 U. S. 608, 37 L. ed. 867, 13 S. Ct. 906."

It will be observed that *Yonley v. Lavender*, 21 Wall. 276, 22 L. Ed. 536, and *Byers v. McAuley*, 149 U. S. 608, 37 L. Ed. 867, cases which clearly establish the propriety of the decree of this case, are cited with approval. These cases are not overruled. When proper Federal jurisdiction exists, the Federal courts are not obliged to defer to a state court in determining a question of a complainant's right merely because *distribution* will be

made in another court. It has been the policy of the Comptroller of the Curreny to direct that all litigation involving the winding up of the affairs of national banks be instituted in the Federal courts to the end that the office charged with this important function of liquidation may secure uniformity of precedents and procedure. The wisdom of such a policy is apparent.

The opinion in the case at bar does not conflict with the opinion of the Circuit Court of Appeals for the First Circuit in *People's Trust Company v. United States,* 23 Fed. (2d) 381, as stated by Petitioners at page 15 of the Petition. In that case, the complainant, before filing his bill in the Federal Court, presented his claim to the officer of the State Court, and it had been allowed but not as a prior claim. In the case at bar, Respondent never presented his claim to the Orphans' Court. The Respondent desired to be relieved of the custody and administration of the Mortgage Pool and did not object to the appointment of a successor Trustee (R. 29-30). The substitution was made to simplify the liquidation of the Bank by relieving Respondent of the administration of the Mortgage Pool. Neither at that time, nor at any time since, has there been any intent or attempt to raise in the State Court any question as to the claim of the Bank.

When the successor Trustee secured orders permitting it to make distribution, the orders directed that payments to Respondent "be suspended pending a judicial determination of the rights of the plaintiff to participate in such distribution" (R. 9, 31, 32) without stating in what jurisdiction the rights of the Respondent should be determined. Respondent took no action in the State Court but proceeded to secure "a judicial determination" of his rights by filing a bill in the District Court. He has never asked the State Court to pass upon

his claim, and it never attempted to allow it, reject it or pass upon it. In the Peoples Trust Company case, the claim was not only presented to the State Court but allowed by it before the bill was filed in the District Court. There the complainant was asking the District Court to pass upon the very same question which he had already raised in the State Court and to overrule the action of the State Court on the question he had presented to it.

II.

The Case Was Properly Determined on the Merits. This involves Points IV and V of the Petition.

(A)

THE ALLOWANCE OF INTEREST IS NOT IN CONFLICT WITH THE DECISION OF THE CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

The decree for the payment of interest advanced by the Bank to the Mortgage Pool does not conflict with the result reached or the opinion rendered in *First Trust Company of Lincoln v. Ricketts,* 75 Fed. (2d) 309 (C. C. A. 8th). In that case a bankrupt had sold coupon notes secured by a mortgage held by it as trustee. The mortgagor ceased paying interest September 30, 1929, foreclosure was instituted by the bankrupt and it secured a deed for the property on February 2, 1931. Despite the fact that the trustee had title to the property, and that interest would never be paid, it continued to pay the coupons until March, 1932, without informing the parties presenting the coupons that title had been acquired by it.

There are several obvious distinctions between the cited case and the case at bar. The holders of participations in the Mortgage Pool did not hold coupons repre-

senting interest on a particular mortgage, nor were they the owners of any particular mortgage or shares in particular mortgages. The aggregate income due participants on the interest date, August 15th, last preceding the date of closing, September 21st, exceeded interest collected by $57,156.76, and this amount was *advanced* or *loaned* to the Mortgage Pool by the Bank. The advancement had been reduced to $40,213.58 at the time of suspension by reason of collections of interest, and the decree provides that the Bank is entitled to be repaid this balance *out of interest collected subsequent to closing* (R. 40). Any ruling other than that made by the District Court would enrich the participants in the Pool at the expense of depositors and other creditors of the Bank by giving participants the Bank's money, and this despite the fact that their contract does not so provide. In the cited case coupons on a *specific mortgage* were paid for two years after the trustee *knew that interest would not be received,* and the trustee held title to the property; while in the case at bar, there was merely a temporary advancement on collections reasonably anticipated with no thought at the time that the Bank would close or that the interest received on the mortgages would not be used to repay the advancement.

The necessity for the temporary advancement is apparent. The mortgages in the Mortgage Pool called for the payment of interest semi-annually, while interest was disbursed quarterly on the Participation Certificates. The Bank closed approximately one month after the date of an interest period, and this resulted in a cessation of the repayments of interest to the Bank when received by the Mortgage Pool. There is no suggestion in the record that there was any attempt to mislead or deceive by paying out interest which was not being earned.

(B)

THE OPERATION OF THE MORTGAGE POOL WAS LAWFUL AND NO QUESTION OF IMPROPRIETY IS PRESENTED BY THE RECORD.

Petitioner's argument that the operation of the Mortgage Pool was unlawful might properly be disposed of by merely pointing out that no such question was raised in the District Court or in the Circuit Court of Appeals until the filing of the Petition for Reargument.

Edward Hines Yellow Pine Trustees v. Martin, 264 U. S. 458, above cited.

In the second place, the operation of the Mortgage Pool was lawful. It is stipulated in the Agreed Statement of Facts that it was established and maintained under the authority of the Pennsylvania Statute approved April 6, 1925, P. L. 152 (15 P. S. 2514). This statute, until repealed by the Pennsylvania Banking Code in 1933, was applicable to all banking institutions exercising trust powers in the Commonwealth of Pennsylvania. It was an amendment to the Act of May 9, 1889, P. L. 159, which amended the General Incorporation Act of April 29, 1874, P. L. 73. Under an opinion of the Attorney General of Pennsylvania, dated June 26, 1918, and reported in 27 District Reports 986, national banks exercising trust powers were required to comply with state regulations for the conduct of such business and were required to file the certificate of acceptance required by the Act of 1889, *supra*. The Bank was authorized by the Federal Reserve Board and by the Secretary of Banking of Pennsylvania to exercise trust powers in that State (R. 25). Section 11 (k) of the Federal Reserve Act (12 U. S. C. A. 248 (k)), merely provides that national banks exercising trust powers "shall segregate all assets held in any fiduciary capacity

from the general assets of the Bank", and it was stipulated by the parties that the Mortgage Pool was "segregated from the general assets of the Bank" (R. 26).

Petitioners say that the Bank sold to the Mortgage Pool participating interests in mortgages owned by it (Petition, page 20). There is not a word in the record to justify this statement and it is not the fact. The mortgages held in the Pool were purchased for the Pool and while they were taken in the name of the Bank as mortgagee, it immediately executed a certificate that the mortgage was held for the Mortgage Pool (R. 26). The Bank did not own the Mortgage Pool but the mortgages in it were held in its trust department for the participants in the Pool. The situation was the same as though the Bank had purchased from third persons for trusts in its trust department, bonds of a corporation issued under a mortgage to the Bank as Trustee.

Again departing from the record because of the attempt to raise the question at this stage of the proceedings, and, as has been previously pointed out, Respondent has filed accounts in all but a few cases, and the question of the propriety of the operation of the Mortgage Pool has not been raised in a single instance. Respondent has examined the files and records of the Bank for any indication of criticism and has found none. The Pool was operated with the full knowledge of the Comptroller of the Currency and without objection by him. Such mortgage pools were conducted by many banking institutions, both state and national, operating in Pennsylvania and were considered as beneficial and desirable by offering a source of sound investment without the delay of finding specific mortgages in varying amounts.

Petitioners quote from what is stated to be a ruling of the Federal Reserve Board as to mortgage pools, but is in fact a summary set out in the Federal Reserve Bul-

letin of March, 1933, at page 187. It will be observed that this ruling was published a year and a half after suspension of the Bank. It does not purport to be based on a decision of any court on the right to operate a mortgage pool but is merely for the guidance of bank officials. It is not contended that this was brought to the attention of the officers of the Bank; and even if this ruling conclusively established the illegality of the Pool, it would at most, as before pointed out, give to holders of certificates a right of action against the Bank and not give the certificate holders a lien on the interest of the Bank in the Pool.

The case of *Larsen v. Bank & Trust Company,* 178 Minn. 209, cited by Petitioners, does not apply because in that case the Trust Company acquired the mortgages in question for itself and not for the trust estate. It executed no declaration of trust, as in the present case, and the Court held that it had not followed the statutory requirements.

Ulmer v. Fulton, Superintendent of Banks, 129 Ohio State 323, is also easily distinguished, as in it the Bank merely set aside as a trust fund certain mortgages and bonds owned by it, acting both as settlor and trustee, which the Court held to be illegal. In that case the Court held that the holders of participation certificates were general creditors of the Bank, which is directly contrary to Petitioners' position in this case. As above stated, if the certificate holders are general creditors, they have no preferred rights with respect to the Mortgage Pool assets.

Primeau v. Granfield, 193 Fed. 911 (C. C. A. 2nd) (1911), is, of course, beside the point. That case holds that the court will not enforce a fraudulent transaction knowingly entered into by the parties, although the

question was not raised in the pleadings in the district court.

The question of legality cannot now be raised and is without merit or existence in fact.

III.

All the Indispensable Parties Were Before the Court.

Petitioners quote the allegation of the Bill to the effect that individuals "are joined herein as defendants as representatives of all holders of certificates issued by the Bank of Pittsburgh against said fund of mortgages, the holders of such certificates being so numerous and so widely scattered that it would be impracticable to bring them all before the Court in this proceeding, and the rights of all certificate holders being the same", but fail to point out that this allegation is admitted by the Answer (R. 14), and that the same facts are stipulated by the parties in the Agreed Statement of Facts (R. 25). Under such circumstances, Petitioners' statement that the defendants are not representatives of a class, and that the interest of the participants cannot be presumed to be the same, is directly in conflict with their admissions in the record.

More than four hundred certificate holders were involved and this situation falls squarely within Equity Rule 38, which provides:

> "When the question is one of common or general interest to many persons constituting a class so numerous as to make it impracticable to bring them all before the court, one or more may sue or defend for the whole."

If additional authority is needed, it may be found in *Kerrison v. Stewart,* 93 U. S. 155, 23 L. Ed. 843 (1876), and *Smith v. Swormstedt,* 16 How. 288, 14 L. Ed. 942

(1853). The question as to the lack of necessary parties was not raised until the filing of the Petition for Reargument in the Circuit Court of Appeals, and is not only tardy but without merit. There is authority for the proposition that an action against the Trustee alone as the representative of all certificate holders would have been proper, but in view of the joinder of certain of the beneficiaries as representatives of all, with the admission in the pleadings and the stipulation of facts that the rights of all are the same, and the class too numerous to join, and the fact that the Trustee which is a party represents at least constructively all of the certificate holders, the question is beyond any serious dispute. Petitioners' authorities clearly have no application to the facts disclosed by this record and require no further discussion.

Respondent respectfully submits the Petition should be denied.

JOHN G. FRAZER,
Counsel for Respondent.

ROBERT L. KIRKPATRICK;
Of Counsel.